4.4 INCOMPATIBLE USES – CRL SECTION 33031 (A) (3)

Section 33031(a)(3) of the CRL identifies one of the physical blight characteristics as adjacent or nearby uses that are incompatible with each other, and which prevent economic development.

The piecemeal development of the Project Area not only helped make it an area filled with obsolete uses, inadequate infrastructure, and poorly maintained properties, but has also helped create changing land use patterns and, in turn, incompatible land uses.

Incompatible uses essentially take two forms in the Project Area: first, where conflicting land uses are located in close proximity to one another without adequate buffers; and second, where current uses are incompatible with the uses called for by the General Plan. Both types of incompatibility substantially impact the ability to improve the Project Area and are extremely difficult to alleviate without redevelopment due to high costs and lack of authority. Overall, 286 properties are affected by these conditions.

Incompatible Adjacent Land Uses

Examples of incompatible land uses exist throughout the Project Area, where parcels have uses that are not compatible with their neighbors. These situations occur primarily because of the way the Project Area has developed through the years. That is, as specific properties transitioned from residential to commercial and industrial, adjacent parcels often remained residential.

This mix of land uses is incompatible because of conflicting traffic patterns, noise impacts, odors, or other nuisances that tend to have attendant health and safety concerns. The result is an area that is not conducive to either residential or business uses. This is a clear demonstration of how the economic development of properties is prevented due to the physical arrangement and layout of existing uses.

Without redevelopment incentives, the abatement of incompatible uses is highly unlikely, because owners, especially absentee owners, are unlikely to invest money in such properties as to eliminate any incompatibilities by replacing one use for another, through screening, or through any other means. In addition to having smaller structures, these lots are themselves relatively small, making conversion to more intense commercial use impossible without parcel assembly. Consequently, the transformation of incompatible uses and irregular parcels into an area more easily developed for its intended uses is unfeasible and, therefore, is a substantial burden on the community.

Incompatible with Planned Land Uses

Incompatible uses related to planned uses were also observed in the Project Area, where existing uses do not conform to the uses designated in the General Plan. When comparing existing land uses to those in the General Plan, 102 parcels are either residential within areas designated for commercial or industrial uses, or commercial and industrial within areas designated for residential uses.

As discussed previously, incompatible, or nonconforming uses create circulation problems, an increased exposure to pollution, and a visual hodgepodge that does not promote private investment. When these characteristics are present it is obvious that economic development is slowed, if not completely halted.

Properties that are incompatible with planned uses also keeps the City from fully implementing its General Plan. This, by definition, is a burden on the community as the City's goals and objectives cannot be met with incompatible uses.

Non-conforming and incompatible uses have a significant impact on the property values. As shown in Table 10, the value per acre of incompatible and non-conforming property is much lower than those that are compatible and conforming in the Project Area. This demonstrates the negative affect that incompatible and non-conforming uses, which is a physical condition of blight, has on property values, which is an economic condition of blight.

TABLE 10

VALUE PER ACRE FOR INCOMPATIBLE AND NON-CONFORMING USES[13]

TYPE	*VALUE PER ACRE*	*DIFFERENCE*
Conforming	$954,617	n/a
Non-conforming	836,554	-12%

Source: Santa Clara Assessor and GRC Redevelopment Consultants, Inc.

The total value of all incompatible or non-conforming uses in the proposed Project Area is $135,421,440. If these properties were improved to the point that they would be assessed at the same value-per-acre as parcels that are conforming and compatible, the

[13] *Determined by professional observations in the field, and calculated from actual values in the Santa Clara County Assessors Rolls. Comparison is between blighted and non-blighted properties in the Project Area to demonstrate the drain on financial resources.*

total value of the proposed Project Area would increase by over $154,000,000. This, in turn, would generate $1,500,000 annually in additional property taxes that would be received by the Agency and shared with all local taxing agencies due to the requirements of the CRL.

Without redevelopment, the abatement of incompatible and non-conforming uses is highly unlikely, because owners, especially absentee owners, are unlikely to invest money in such properties in such a manner as to eliminate any incompatibilities by replacing one use with another, through screening, or through any other means.

Visually, incompatible or nonconforming uses act as a disincentive for investment, because it is neither the best environment nor the cheapest in which to develop a particular use. In other words, private development dollars flow to the points of least resistance. Unfortunately, there are many points of resistance in the Project Area.

In a similar manner, a commercial lender is less likely to invest in an area of visual and functional hodgepodge than in an area that is prepared for commercial/industrial development. When uses are mixed due to shifting needs and piecemeal development, they generally appear as an unattractive and jumbled mess to be avoided as quickly as possible. In addition, lenders may see loans to blighted areas as high risk, which increases interest rates and, in turn, the costs of development. This clearly demonstrates how blight prevents future investment in an area, inhibits investment, and allows existing uses to stagnate.

Photos C1 – C10 are examples of incompatible and/or non-conforming uses in the Project Area.

Photo C1

- Deterioration
- Incompatible uses
- Missing curb, gutter, and sidewalk

Photo C2

- Incompatible uses
- Need for utility undergrounding
- Illegal signs

Photo C3

- Deterioration
- Incompatible uses
- Barbed wire

Photo C4

- Incompatible uses

Photo C5

- Deterioration
- Vacant and boarded up
- Non-conforming residential use in a commercial area

Photo C6

- Incompatible uses (multi-family structure in a shopping center)

Photo C7

- Incompatible uses

Photo C8

- Deterioration
- Incompatible uses
- Non-conforming mobile homes in a commercial area

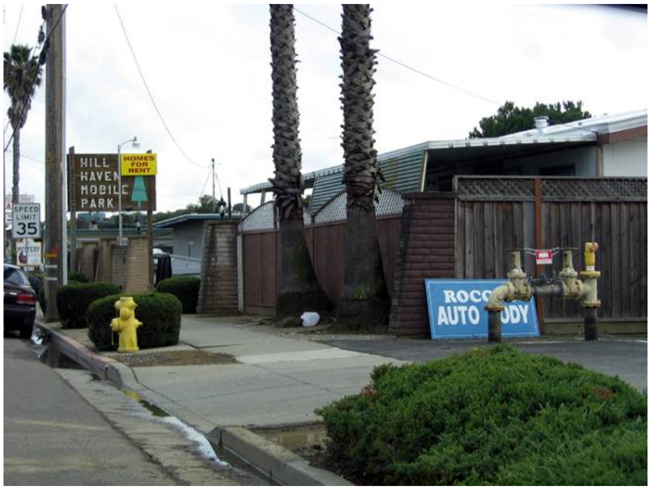


Photo C9

- Incompatible uses (pre-school adjacent to a gas station)

Photo C10

- Incompatible uses
- Non-conforming residences located in a commercial area

4.5 DEPRECIATED VALUES OR IMPAIRED INVESTMENTS – CRL SECTION 33031 (B) (1)

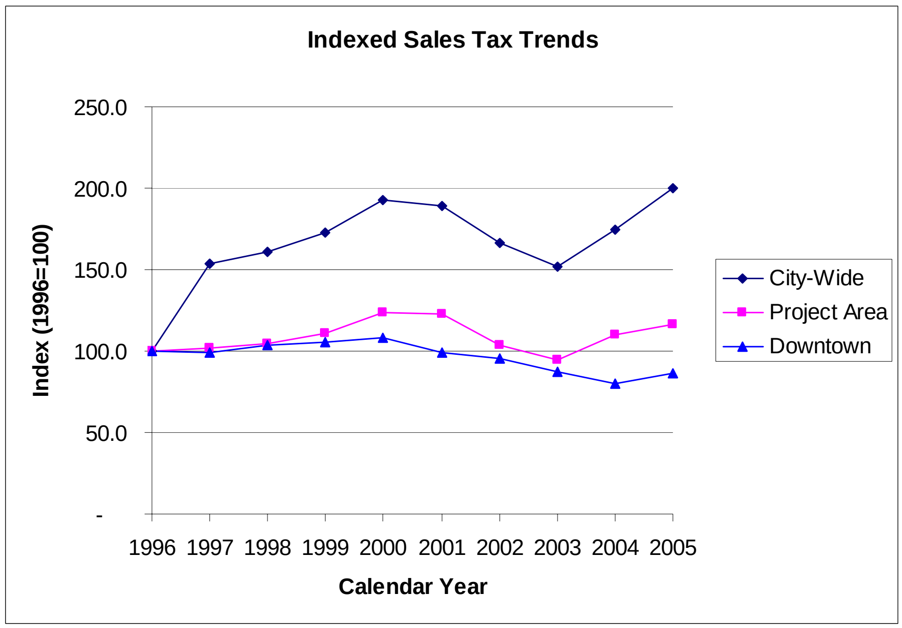
State, County, and local entities levy a sales tax on most retail sales in California. As such, trends in sales tax receipts are a direct measure of performance in the retail economy of an area, and are therefore a good measure of investments.

Short of a significant change in local land uses (e.g., from retail commercial to residential or industrial) or types of economic activity (e.g., types of commercial uses), increasing sales tax receipts are a direct indication of improved taxable sales in an area, while declining receipts tend to indicate a significant decline in the local retail economy. Stagnant retail sales trends indicate stagnation in the health of the local retail sector of the economy.

Stagnating or declining retail sales, in turn, indicate depreciated or stagnant investments in an area. For instance, with decreased sales, the values of businesses also tend to decline, with such businesses having ever-harder times covering the costs of employment and overhead. Lease payments to property owners also tend to be adversely affected in cases where lease payments are indexed in whole or part to sales. As such, the value of the property as an investment declines as it relates to economic activity on the land, and the investment of the property owner is impaired or adversely affected.

Table 11 is an evaluation of sales tax trends in Morgan Hill, the Project Area, and the downtown portion14 of the Project Area for the ten years between 1996 and 2005. Sales numbers in the table were adjusted to account for inflation based on the San Francisco area's Consumer Price Index. As shown, total sales in the downtown area declined by about 14% during the analysis period, while City-Wide sales nearly doubled and Project Area-wide sales increased by 16%.

TABLE 11 – SALES TAX TRENDS



After 2000, the downward trend in retail sales in the downtown area resulted primarily from declines in General Retail sales and from a lesser decline in Transportation-related sales. Project Area-wide, General Retail sales declined after 2002, but were off-set by increases in Transportation and Construction-related sales.

Based on the data in Table 12, which shows sales tax by category, and the above discussion, the downtown area has experienced a significant decline in real, inflation-adjusted, sales in the past decade, which has resulted in an impairment of investments in the area due to declines in economic return. Retail sales in the Project Area as a whole have increased only slightly over the past ten years, and at a much slower rate than the City as a whole. As such, the Project Area as a whole continues to experience nearly-stagnant retail growth rates, and the impaired investments that area likely to result. Unlike the Project Area and the downtown

[14] *Downtown includes the area between Main Avenue, Depot Street, Dunne Avenue, and Del Monte Avenue.*

area, City-wide growth rates have increased significantly, mostly in the Food Products, Transportation-related and Construction-related sectors.

TABLE 12 – SALES TAX BY CATEGORY

SALES TAX HISTORY BY CATEGORY BY CALENDAR YEAR: 1996 THROUGH 2005
($2005)

CITY-WIDE EXCLUDING PROJECT AREA								
Calendar Year	General Retail	Food Products	Transportation	Construction	Business-to-Business	Miscellaneous	Total	Index (1996=100)
2005	$ 951,153	$ 763,095	$ 2,156,969	$ 620,184	$ 692,492	$ 14,494	$ 5,198,387	199.9
2004	$ 939,000	$ 723,929	$ 1,491,701	$ 609,731	$ 738,203	$ 13,255	$ 4,534,240	174.3
2003	$ 1,011,000	$ 674,979	$ 1,302,482	$ 325,104	$ 577,963	$ 15,481	$ 3,939,439	151.5
2002	$ 1,124,000	$ 740,433	$ 1,361,136	$ 340,284	$ 686,869	$ 18,905	$ 4,328,118	166.4
2001	$ 1,138,000	$ 800,553	$ 1,420,715	$ 381,063	$ 1,075,943	$ 29,887	$ 4,922,867	189.3
2000	$ 1,113,000	$ 788,528	$ 1,424,074	$ 464,568	$ 1,055,120	$ 24,747	$ 5,009,007	192.6
1999	$ 1,038,000	$ 775,548	$ 1,271,428	$ 520,557	$ 662,741	$ 30,552	$ 4,480,551	172.3
1998	$ 971,000	$ 764,259	$ 1,087,599	$ 492,359	$ 624,634	$ 34,294	$ 4,192,399	161.2
1997	$ 900,000	$ 754,438	$ 1,056,466	$ 505,486	$ 501,695	$ 39,175	$ 3,994,605	153.6
1996	$ 747,000	$ 471,790	$ 648,222	$ 328,032	$ 160,749	$ 15,683	$ 2,600,729	100.0

RANCHO DE OJO REDEVELOPMENT PROJECT AREA								
Calendar Year	General Retail	Food Products	Transportation	Construction	Business-to-Business	Miscellaneous	Total	Index (1996=100)
2005	$ 538,786	$ 366,450	$ 691,887	$ 540,373	$ 522,052	$ 2,823	$ 2,662,371	116.4
2004	$ 549,865	$ 354,511	$ 505,865	$ 542,053	$ 570,613	$ 3,246	$ 2,526,153	110.4
2003	$ 645,773	$ 347,509	$ 451,020	$ 283,373	$ 422,241	$ 3,496	$ 2,153,412	94.1
2002	$ 754,279	$ 392,572	$ 450,321	$ 278,393	$ 498,797	$ 4,920	$ 2,379,283	104.0
2001	$ 755,377	$ 455,725	$ 433,613	$ 296,397	$ 854,595	$ 8,174	$ 2,803,880	122.5
2000	$ 771,254	$ 450,642	$ 449,484	$ 343,020	$ 809,280	$ 10,069	$ 2,833,749	123.9
1999	$ 756,700	$ 460,068	$ 378,051	$ 405,534	$ 531,164	$ 11,411	$ 2,542,928	111.1
1998	$ 731,286	$ 461,487	$ 293,398	$ 380,652	$ 522,156	$ 9,558	$ 2,398,539	104.8
1997	$ 714,457	$ 473,197	$ 325,270	$ 386,964	$ 410,796	$ 16,486	$ 2,327,170	101.7
1996	$ 713,045	$ 460,027	$ 356,462	$ 337,133	$ 405,409	$ 15,955	$ 2,288,031	100.0

DOWNTOWN PORTION OF RANCHO DE OJO REDEVELOPMENT PROJECT AREA								
Calendar Year	General Retail	Food Products	Transportation	Construction	Business-to-Business	Miscellaneous	Total	Index (1996=100)
2005*	$ 35,582	$ 51,466	$ 23,986	$ -	$ 2,336	$ 5	$ 113,375	86.1
2004	$ 39,168	$ 45,223	$ 19,258	$ 108	$ 1,306	$ 55	$ 105,117	79.8
2003	$ 43,023	$ 48,148	$ 22,115	$ -	$ 1,372	$ 5	$ 114,664	87.1
2002	$ 54,166	$ 48,660	$ 21,604	$ 358	$ 1,253	$ 13	$ 126,053	95.7
2001	$ 55,738	$ 48,139	$ 23,527	$ -	$ 3,216	$ 294	$ 130,913	99.4
2000	$ 64,549	$ 48,342	$ 26,396	$ -	$ 2,940	$ 534	$ 142,762	108.4
1999	$ 57,385	$ 50,022	$ 26,939	$ 342	$ 3,197	$ 944	$ 138,828	105.4
1998	$ 50,407	$ 49,209	$ 32,044	$ 185	$ 4,230	$ 877	$ 136,952	104.0
1997	$ 39,961	$ 49,780	$ 32,619	$ -	$ 7,441	$ 972	$ 130,773	99.3
1996	$ 32,523	$ 45,310	$ 35,544	$ 9,083	$ 7,942	$ 1,303	$ 131,705	100.0

Notes:

Above numbers do not include Morgan Hill's share of State and County sales tax pools and are presented on an economic basis, which excludes current payments of prior taxes due and which includes anticipated unpaid payments for current periods.

Source: MBIA/Muni Services, July 2005. Based on State of California sales tax records.

Another demonstration of depreciated values in the Project Area has already been presented throughout this Chapter. The economic affect blight has on property values is severe and includes:

- Structures that are so deteriorated that they are unsafe or unhealthy to occupy, which are assessed 86% lower than properties in good condition in the Project Area
- Structures that are deteriorated to the point where they are a factor that hinders viable uses, which are assessed 67% lower than properties in good condition in the Project Area
- Obsolete commercial buildings are assessed 55% lower than those with more design elements or updated façades in the Project Area
- Buildings over 30 years old are assessed 66% lower than those less than 30 years old in the Project Area
- Single-family residential properties that are absentee owned are assessed 48% lower than those that are owner-occupied in the Project Area
- Properties with openly stored equipment, junk, and other materials are assessed 78% lower than those that are clean in the Project Area
- Properties with non-conforming or incompatible land uses are assessed 12% lower than those that are conforming or compatible in the Project Area

These examples clearly show depreciated values in the Project Area due to the existence of remaining blight.

4.6 VACANCIES, ABANDONED BUILDINGS, AND LOW LEASE RATES – CRL SECTION 33031 (B) (2)

Section 33031(b)(2) of the CRL identifies several conditions as characteristics of economic blight, including abnormally high business vacancies, abnormally low lease rates, high turnover rates, abandoned buildings, or excessive vacant lots within an area developed for urban use and served by utilities.

Industrial uses in the Project Area are by far the land use category which suffers the most from high vacancies. At 18%, the vacancy rate of these businesses is much higher than the generally accepted norm of 10%. Many of the older industrial buildings in the Project Area have been vacant or predominately vacant for years, which is reflective of the obsolete conditions mentioned earlier in this Chapter.

Vacant businesses illustrate the complex nature of blight. Poor physical conditions lead to decreased values and sales, which, in turn, lead to poor economic conditions. Vacancies not only give the area a run-down look and reduce local job opportunities, but they do not generate sales tax revenue, frequently lower surrounding property values, increase crime and the risk of fire, and pose hazards to children.[15] These are all factors that substantially hinder or prevent viable uses.

Empty buildings exhibiting characteristics of neglect and abandonment such as broken windows, garbage, or other such indications of neglect, are typically regarded as attractive nuisances and neighborhood burdens and often attract transients who commit crimes related to property, intoxication, and illegal occupancy. Additionally, the standard concept of "The Broken Window Effect", which is widely accepted in professional planning literature, points strongly to a very high degree of correlation between apparent building abandonment and crime.[16]

Vacancies have a significant impact on the property values. As shown in Table 11, the value per acre of industrial properties with vacancies is much lower than those that are fully occupied in the Project Area.

TABLE 11

VALUE PER ACRE FOR VACANT INDUSTRIAL USES[17]

TYPE	*VALUE PER ACRE*	*DIFFERENCE*
Occupied	$1,217,479	n/a
Vacant	1,093,441	-10%

Source: Santa Clara Assessor and GRC Redevelopment Consultants, Inc.

The total value of all incompatible or non-conforming uses in the proposed Project Area is $109,606,501. If these properties were improved to the point that they would be assessed at the same value-per-acre as industrial parcels that are fully occupied, the total value of the Project Area would increase by nearly $122,000,000. This, in turn, would generate over $1,200,000 annually in additional property taxes that would be received by

[15] *Kraut, David T., "Hanging Out the No Vacancy Sign: Eliminating the Blight of Vacant Buildings from Urban Areas", New York University Law Review, New York, New York, October, 1999.*

[16] *Wilson, James Q. and Kelling, George L., "Broken Windows",* The Atlantic*, Boston, Mass., March, 1982.*

[17] *Determined by professional observations in the field, and calculated from actual values in the Santa Clara County Assessors Rolls. Comparison is between blighted and non-blighted properties in the Project Area to demonstrate the drain on financial resources.*

the Agency and shared with all local taxing agencies due to the requirements of the CRL.

Successful continuation of the redevelopment program will address the vacancies by providing incentives to attract new businesses, or facilitating parcel assembly, which could create properties that are viable in today's market.

Photos D1 – D32 are examples of vacancies in the Project Area.

Photo D1

- Vacant commercial unit

Photo D2

- Vacant industrial unit

Photo D3

- Vacant industrial building

Photo D4

- Vacant industrial building

Photo D5

- Vacant office space

Photo D6

- Vacant industrial building

Photo D7

- Vacant industrial building
- No landscaping

Photo D8

- Vacant industrial building

Photo D9

- Vacant office building

Photo D10

- Vacant industrial building

Photo D11

- Vacant industrial building
- Inadequate parking area

Photo D12

- Vacant commercial building
- Barbed wire
- Overgrown weeds
- Graffiti

Photo D13

- Vacant office unit

Photo D14

- Vacant commercial unit

Photo D15

- Vacant commercial units

Photo D16

- Vacant single-family home
- Significant deterioration

Photo D17

- Vacant industrial building

Photo D18

- Vacant commercial unit

Photo D19

- Vacant commercial building

Photo D20

- Vacant office unit

Photo D21

- Vacant office building

Photo D22

- Vacant industrial building

Photo D23

- Vacant office space

Photo D24

- Vacant industrial building

Photo D25

- Vacant industrial building

Photo D26

- Vacant industrial building

Photo D27

- Vacant industrial building

Photo D28

- Vacant commercial unit

Photo D29

- Vacant industrial building

Photo D30

- Vacant industrial building

Photo D31

- Vacant commercial space

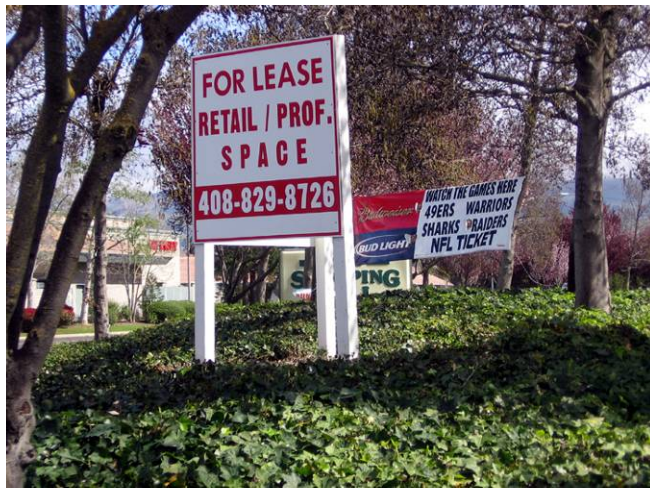


Photo D32

- Vacant industrial space

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5.0 SUMMARY OF REMAINING BLIGHT

As shown in the matrix below, characteristics of three categories of physical blight and two categories of economic blight were observed in the Project Area. These combined conditions of significant remaining blight are spread throughout the Project Area (see Figure 6).

TYPE OF BLIGHT DEFINED BY THE CRL	REMAINS SIGNIFICANT IN PROJECT AREA?	EXAMPLES
Physical - 33031 (a) (1)	Yes	Dilapidation, flooding, hazardous materials, code violations
Physical - 33031 (a) (2)	Yes	Deterioration, obsolescence, absentee ownership, inadequate infrastructure
Physical - 33031 (a) (3)	Yes	Incompatible adjacent land uses, non-conforming uses
Economic - 33031 (b) (1)	Yes	Retail sales in Downtown declined 14% while Citywide retail sales nearly doubled
Economic - 33031 (b) (2)	Yes	High rate of industrial vacancies

The following is a summary of the physical and economic conditions of blight described in the previous Chapter:

- Approximately 32% of the properties are located in a FEMA flood zone
- Groundwater contamination from the Olin site has cost Morgan Hill taxpayers approximately $3,000,000 and the problem is still unresolved
- Nearly 350 properties have structures that are in some degree of disrepair, with nine properties in serious dilapidation

- Properties with dilapidated structures are assessed over seven times lower than of those in good condition
- Properties with structures that need renovation are assessed nearly three times lower than those in good condition
- Over 800 buildings are likely to contain such hazards as asbestos and/or lead paint
- Approximately 60% of all code enforcement complaints come from the Project Area, despite being only 38% of the City's land area
- Over 70 properties have obsolete structures
- Properties with obsolete structures are assessed over two times lower than of those that are not obsolete
- Over 950 structures are over 30 years old
- Properties with structures over 30 years old are assessed nearly three times lower than of those under 30 years old
- Absentee ownership rate for single-family residences is 19%, compared to the Citywide rate of 13%
- Absentee owned single-family residences are seven times likely to be deteriorated or dilapidated than those that are owner-occupied
- Absentee owners are located in 22 states across the country
- Properties with single-family homes owned by absentee owners are assessed nearly two times lower than of those that are owner-occupied
- About $96,000,000 is needed for infrastructure deficiencies
- Properties with outdoor storage of equipment or materials are assessed almost five times lower than of those without outdoor storage
- Nearly 290 properties are non-conforming or incompatible with adjacent land uses
- Properties that are non-conforming or incompatible are assessed less than of those that are conforming or compatible
- Retail sales down 14% in Downtown compared with an increase of nearly double for the entire City
- The vacancy rate on industrial properties is 18%
- Industrial properties with vacancies are assessed less than of those that are fully occupied

Burden on the Community

Examples were presented throughout Chapter 4.0 showing the negative affect remaining blight has on property values in the Project

Area. In just those examples alone, the average blighted property is assessed 53% lower than non-blighted property. When combined with the fact that the Project Area is home to 60% of all Citywide code violation complaints and nearly $100,000,000 of infrastructure improvement needs, it is clear that the Project Area is a drain on City resources. The problem is further compounded when considering the extra resources spent on blighted properties due to flood damage, hazardous material clean-up, and other conditions described throughout the previous chapter. Thus, the remaining blight is a substantial burden on the community.

In addition, because of the lower assessed values due to blighted property, the Project Area does not generate enough revenue to overcome the blight unless redevelopment is allowed to continue. In other words, the properties with remaining blight do not "pay their fair share" of the property tax burden. In fact, non-blighted properties must, in essence, subsidize the blighted property because the lost revenues must be made up through other sources.

In using just the examples identified in this Report, blighted properties are assessed over $1,129,000,000 lower than non-blighted properties in the Project Area. The Agency and other taxing entities, such as the City and the County, lose over $11,000,000 each year in property tax revenues that could be received if blight did not exist.

The revenues lost by having so many blighted properties remaining in the Project Area drains City resources that could be applied to remediation of other unidentified problems, or to other governmental services. This shows how the Morgan Hill community as a whole is burdened by the blight that remains in the Project Area.

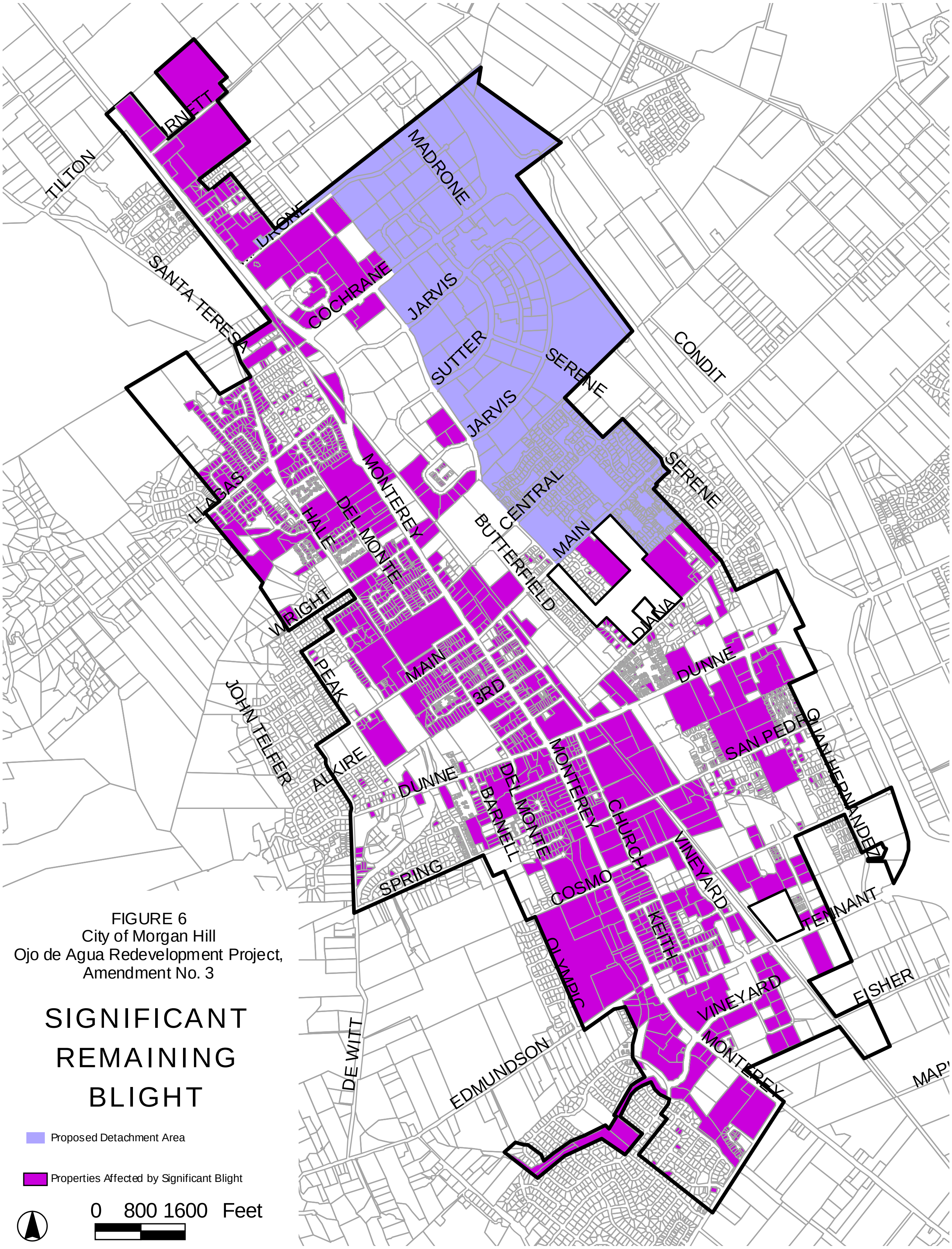

FIGURE 6
City of Morgan Hill
Ojo de Agua Redevelopment Project,
Amendment No. 3

SIGNIFICANT REMAINING BLIGHT

6.0 DESCRIPTION OF PROPOSED PROJECTS OR PROGRAMS AND HOW THEY WILL ELIMINATE OR ALLEVIATE BLIGHT

The CRL requires that a Preliminary Report include a description of the specific projects and programs to be undertaken by the Agency and how these programs and project will alleviate blight in the Project Area. This section provides this information..

The specific projects and programs proposed by the Agency to eliminate the remaining blight in the Project Area include those described below.

Economic Revitalization Programs

The Agency intends to encourage new commercial, mixed use, and industrial development in the Project Area through this program. Under this program, the Agency can enter into public/private partnerships by assisting with land assembly, site preparation, offsite improvements, disposition of property, hazardous waste remediation and relocation assistance to existing property owners and tenants. The Agency may also acquire property and resell it to developers at the reuse value of the property. Another component of this program includes the development of marketing materials to attract and retain businesses in the Project Area.

The program also encourages existing property owners and businesses to upgrade the exterior of buildings, correct code violations and renovate the interior of stores. The program provides deferred payment and low interest loans to property owners to make the types of improvements described above. Expenses are also reimbursed to business owners for façade improvements. Historically important buildings can also be preserved through this program.

Although the Agency does not have any specific projects in mind, the program will most likely be focused on those areas where significant deterioration and dilapidation exist. This includes the following general locations:

- Mast Street west of Vineyard Boulevard
- Tennant Avenue east and west of Church Street
- Dunne Avenue west of Lotus Way
- Monterey Road at Wright Avenue
- Monterey north of Spring Avenue
- Del Monte Avenue north of West Dunne Avenue

The program will also be used to implement the various goals contained in the Downtown Specific Plan that was approved in April 2003. The Specific Plan envisions the strengthening of the Downtown area as the social and cultural heart of the City. A diverse set of uses are to be encouraged, including specialty retail, entertainment and restaurant uses. Infill development is also encouraged in the Plan, as is the rehabilitation of existing uses. Improvements to the circulation system and additional parking will be needed to implement the Specific Plan.

The Economic Revitalization Program will assist in the elimination of blight in a number of areas, including removal or rehabilitation of the most obsolete structures in the Project Area. This program would address a variety of physical blighting conditions, including deterioration, dilapidation, obsolescence, and the removal of hazardous materials. The Program will also assist in the alleviation of economic blight by reversing conditions of impaired investment and, thus, encourage private investment.

Street, Flood Control, Water, and Sewer Projects

The Agency intends to fund improvements designed to strengthen the Project Area. These projects are either directly related to the alleviation of blight, such as improvements to the flood control system, or are needed in order set the economic environment in which private sector reinvestment can occur.

Major circulation improvements may include one or more of the following projects:

- Madrone/Monterey Improvements
- Dunne Grade Separation
- Dunne Widening

- Butterfield Extension (s/o Tennant to Monterey Road), possible Widening and Grade Separation
- Tennant Ave. Widening
- Tennant Ave/101 Overcrossing/Expansion
- San Pedro/Spring Realignment
- Street Construction/Reconstruction
- Median Construction: Monterey & Cochrane
- Downtown Traffic Calming
- Santa Teresa Blvd Construction
- Madrone UPRR Overcrossing
- Traffic Signals
- Undergrounding Monterey Road Utilities
- Other Utility Undergrounding
- Sidewalk Construction
- Other Street Improvements & Extensions

Traffic and circulation problems have affected the Project Area for a number of years, so it is important to address dilapidated streets, install missing sidewalks, and make other modifications that are needed to eliminate safety issues. For example, the installation of the Dunne Avenue under crossing is directly related to public safety because vehicles would no longer be required to cross the railroad tracks, which improves response times for police and fire vehicles. The construction of medians provides for safer traffic turn movements.

Many of the planned circulation improvements are of area wide importance but will also assist in the revitalization of the Project Area. For example, the extension of Butterfield Boulevard south of Tennant Avenue and the grade separation is needed in order to ease traffic on Monterey Road. This would help to achieve one of the goals of the Downtown Specific Plan, which is to reduce traffic on Monterey Road, thereby making the Downtown more pedestrian- and retail-friendly. Furthermore, this would improve north/south circulation throughout the Project Area, and provide a safer alternative to crossing the railroad tracks.

The Tennant Avenue overcrossing would eliminate traffic bottlenecks for a primary east/west roadway, and enhance the development of property in the Project Area.

Flood control improvements are of vital importance in the Project Area, and include the following types of projects:

- PL 566 Regional Flood Control Project for West Little Llagas Creek
- Local Connections
- Butterfield Storm Drain

As explained in Chapter 4.0, flood risk is high for a large percentage of the properties in the Project Area. Correcting the inadequacies in the flood control system will likely save millions of dollars in flood damage and possibly the lives of those in danger. Adequate flood control will also open new investment opportunities, particularly along Monterey Road and in the Downtown area. In fact, major redevelopment in the Downtown area cannot take place until PL 566 is constructed. While most of the cost for this improvement is to be born by the federal and state governments, redevelopment financing may be needed to provide gap funding or to serve as a local match.

Water and sewer improvements are necessary to maintain the health and safety of all Morgan Hill residents and employees. Such improvements could include reconstruction of sewer mains and various upgrades to the water system. As with the flood control facilities mentioned above, inadequate water and sewer lines are a deterrent to investment. Therefore, it is critical that these systems be improved.

In summary, the public improvement program will fund improvements designed to reduce flooding in the Project Area. The Project Area also has major sewer and water line deficiencies that are hindering the economic development of these properties. Agency assistance with these improvements will help foster industrial, commercial and residential development in the Project Area. Finally, infrastructure improvements related to vehicular circulation will alleviate traffic congestion. Each of these types of improvements establishes an environment in which private sector investment can occur, which leads to further blight alleviation.

Community Facilities Projects

The following types of community facilities are proposed to be constructed in the Project Area:

- Library Expansion
- Aquatics Center Improvements
- Sports Complex Implementation

- Youth Center (renovation El Toro/Friendly Inn)
- Community Park Master Plan Implementation, including Corporation Yard Relocation
- Fire Station

A key factor of any successful community is the services and facilities it provides. Until recently, such facilities in Morgan Hill have been obsolete or even non-existent. Improvements have been made, but more work is needed because a higher quality of life tends to attract more investment into the Project Area. This would address obsolescence, vacancies, and impaired investments.

Housing Programs

The Housing Program will continue to implement one of the major goals of the CRL, which is to increase, improve, and preserve low- and moderate-income housing. The Agency has had a very pro-active housing program in the past and had implemented the following types of projects:

- Housing Rehab Loan Program
- Senior Housing Repair Program
- Mobile Home Repair Program
- New Housing Development
- Major Housing Rehab Projects
- BMR Program Administration

In attaining this goal, the Agency will also alleviate certain blighting conditions in the Project Area, such as unsafe or unhealthy buildings, vacancies, deterioration, and impaired investments. Development of new and the rehabilitation of existing housing will also enhance the economic vitality of the Project Area and the entire City.

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7.0 REASONS BLIGHT CANNOT BE ALLEVIATED WITHOUT EXTENDING LIMITS

The provisions of the CRL require that when an agency proposes to increase and extend the financial limitations of an existing redevelopment plan, it must identify the remaining blight within the project area, identify the portion, if any, that is no longer blighted, and identify the projects that are needed to eradicate the remaining blight. In addition, the relationship between the costs of those projects and the amount of increase in the limitation on the number of dollars proposed to be allocated to the agency must be shown. The City Council must also make a finding that:

1. Significant blight remains within the project area, and
2. The blight cannot be eliminated without the establishment of additional debt and the increase in the limitation on the number of dollars to be allocated to the agency.

The Agency's proposed amendment includes an increase in the number of dollars to be allocated to the Agency (tax increment limit) , the re-establishment of the authority to issue tax allocation bonds, and an increase in the bond limit. These amendments are needed in order to fund redevelopment program activities and eliminate remaining blight. Without the amendment, the Agency will have very little financial capacity to fund additional redevelopment activities. As of the start of the 2005-06 fiscal year, the Agency had only $52 million in remaining tax increment that it could collect under the current $247 million limit. All but about $6 million of these funds have either been expended or are committed to complete certain projects of the Agency, including:

- The construction of the library, which will use approximately $13 million of the remaining limit;

- The completion of the Centennial Recreation Center which is estimated to use $19.2 million of the remaining limit;
- The required deposit to the housing fund of approximately $10 million;
- Other obligations of the Agency, including administrative expenses, that are estimated to use $4 million

Because the current tax increment limit is so low, and the inability for the Agency to issue bonds, the Agency has no ability to generate additional capital to finance improvements, since almost all of the current tax increment is committed to existing obligations. The total estimated cost of the Agency's program of redevelopment (in today's dollars) is over $231 million. This cost does not include inflationary impacts or additional interest costs that could be incurred when funds are borrowed. Without an amendment to the tax increment limit, the Agency will be unable to continue to implement a program of redevelopment designed to alleviate blight.

Despite the efforts of the Agency, the Project Area continues to suffer from physical and economic blighting conditions which cannot reasonably be expected to be removed by the private sector acting alone. These remaining blighting conditions are discussed in earlier sections of this Report. In light of the extensive role the Agency needs to take in implementing the continuing redevelopment programs, redevelopment efforts will need to extend well into the current century. The amendment of the financial limits of the existing Redevelopment Plan is necessary to fund the continued redevelopment program as proposed in this Report.

The re-establishment of bonding capacity is also essential if the Agency is to remove remaining blight. The deletion of territory from the Project Area will reduce the annual flow of tax increment by over $7 million per year. In order to continue to implement redevelopment activities in a timely manner, it will be necessary for the Agency to issue tax allocation bonds. This will allow the Agency to generate a large amount of capital to fund projects. The current bond limit was set at $7 million, and this was only to cover bonds that were outstanding in 1999 when the last amendment to the Redevelopment Plan took place. Under the current Redevelopment Plan, the Agency has no authority to issue new bonds.

The Agency intends to continue its pro-active program of redevelopment in order to continue to alleviate blight and create and improve affordable housing in the Project Area. The cost of that program, when combined with the current obligations in the Project Area, will exceed $557 million, as shown on Table 5. Given the remaining needs of the Project Area, and the lack of other ongoing funding sources, the Agency will need to look to tax increment financing as a major source of funding. Neither the City nor the private sector has historically been able to finance the types of redevelopment efforts that are needed in the Project Area.

As required by the CRL, the City and the Agency will continue to look to other funding sources to assist in the redevelopment effort. The Agency is, in fact, assuming that a portion of the future costs for redevelopment will come from sources other than tax increment, including development impact fees and private sector resources. However, tax increment is needed to fill funding gaps between the costs identified and these other funding sources.

Historically, other funding sources have also not been sufficient to alleviate blight in the Project Area. Also, if the levels of assessments or development impact fees are too high, this can increase the costs for private development and further discourage blight remediation. This has, in fact, been the case in the Project Area. In addition, development impact fees can only be set at a level to cover the impacts that are created by the development and cannot be used to raise additional funds to remove existing deficiencies in the Project Area.

In summary, the current financial limits restrict the Agency's ability to issue new debt or to finance projects and programs. By increasing the tax increment limit and re-establishing the authority of issue bonds, the Agency will have the financial resources to complete an effective redevelopment program aimed at eliminating remaining blight and constraints to development throughout the Project Area. The Agency will have a very limited ability to assist in the elimination of remaining blight unless the existing financial limits are increased by adoption of the proposed amendments.

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8.0 PROPOSED METHOD OF FINANCING AND FEASIBILITY OF THE AMENDMENT

Section 33344.5 (d) of the CRL requires that a Preliminary Report include information on the proposed method of financing the redevelopment plan, including information on the economic feasibility of the Redevelopment Project Area and the reasons for including tax increment financing. This Section 8.0 includes information on the estimated costs of the program of redevelopment; describes the various financing sources that may be used; demonstrates the continued economic feasibility of the Project Area; and describes the reasons for continuing to include tax increment financing in the Redevelopment Plan.

The financial projections shown in this section are for illustrative purposes only and do not reflect any approved policy direction by the Agency Board. As such, they are not meant to indicate any future Agency actions. The projections have been prepared for the sole purpose of determining whether the amended Redevelopment Plan will be financially feasible.

8.1 REDEVELOPMENT PROGRAM COSTS

The costs to continue to implement the redevelopment program are summarized on Table 12. The costs on Table 12 are shown in current (2006) dollars, which are estimates and subject to change. The estimated costs are grouped by major program category, with a list of specific projects or activities that may take place within each. The cost shown on Table 12 reflects only the portion of funding expected to be available from the Agency's tax increment revenue stream. The total cost for all of the programs and projects shown on Table 12 is estimated at over $500 million. Of this amount, tax increment is anticipated to provide funding of $231 million.

Chapter 6.0 of this Report provides information on the Agency's program of redevelopment and its relationship to blight alleviation. In addition to the program costs shown on Table 12, the Agency will need to incur expenses for administration of the Project Area. Such costs will include staff time, legal and technical assistance, and the preparation of planning studies and reports.

The total cost for the Agency's revitalization effort is estimated at $229 million in 2006 dollars. This amount does not include the impacts of inflation or the interest costs associated with the borrowing of funds to continue to implement the redevelopment program. It also does not include mandatory payments to the taxing entities. The mandatory payments are required by the CRL due to a prior amendment to the Redevelopment Plan. Each of these additional items has been included on Table 16 and Appendix B, which reflects the overall analysis of the Project Area's economic feasibility.

Table 12
Morgan Hill Redevelopment Agency
Ojo de Agua Project Area

PROJECTS AND PROGRAMS - CURRENT DOLLARS (1)
(000'S Omitted)

Economic Revitalization
- Marketing
- Foster Business Attraction & Retention
- Projects & Programs to Enhance Downtown
- Façade Improvement Program
- Commercial Rehab. Loan Program
- Historic Preservation
- Entry Statement Construction
- Toxic Clean-up
- Downtown Off-Street Parking Improvements
- Downtown Streetscape/Ped Improvements
- Third Street Promenade & Plaza

Total	**63,000,000**

Street Improvements
- Madrone/Monterey Improvements
- Dunne Grade Separation
- Butterfield Extension (s/o Tennant to Monterey Road), possible widening and grade separation
- Tennant Ave. Widening
- Tennant Ave. Overcrossing Expansion
- San Pedro/Spring Realignment
- Street Construction/Reconstruction
- Median Construction: Monterey & Cochrane
- Downtown Traffic Calming
- Santa Teresa Blvd Construction
- Madrone UPRR Overcrossing
- Traffic Signals
- Undergrounding Monterey Road Utilities
- Other Utility Undergrounding
- Sidewalk Construction
- Other Street Improvements & Extensions

Total	**48,000,000**

Flood Control
- PL 566
- Local Connections
- Butterfield Storm Drain

Total	**22,000,000**

Table 12
PROJECTS AND PROGRAMS - CURRENT DOLLARS (1)
Page 2

Water/Sewer	
Sewer Main Reconstruction	
Water System (Mains, New Wells, Pumping Station)	
Total	**6,000,000**
Community Facilities	
Library Expansion	
Aquatics Center Improvements	
Sports Complex Implementation	
Youth Center (renovation El Toro/Friendly Inn)	
Community Park Master Plan Implementation, including Corporation Yard Relocation	
Fire Station	
Total	**20,000,000**
TOTAL NON HOUSING PROGRAM COSTS	**159,000,000**
Affordable Housing Programs	
Housing Rehab Loan Program	
Senior Housing Repair Program	
Mobile Home Repair Program	
New Housing Development	
Major Housing Rehab Projects	
BMR Program Administration	
Total	**70,000,000**
GRAND TOTAL -- ALL PROGRAMS	**229,000,000**

(1) Assumes partial Agency funding for most projects.

8.2 FINANCING METHODS AND ALTERNATIVES AVAILABLE TO FUND REDEVELOPMENT

The proposed amendment to the Redevelopment Plan will, among other things, increase the tax increment limit, and re-establish bonding authority in the Project Area. The proposed amendment also includes the deletion of territory from the Project Area.

The amendment does not affect the Agency's authority to fund activities from a variety of sources, including:

- Financial assistance from the City, the State and the federal government
- Tax increment funds
- Agency bonds
- Donations
- Special assessment districts
- Interest income
- Loans from private financial institutions
- The lease or sale of Agency owned property
- Any other legally available public or private sources of funding.

The Agency is also authorized to obtain advances, borrow funds and create indebtedness in various forms, including bonds. However, the current bond limit, of only $7,000,000, is too low for any significant improvement project. In addition, the Agency may not establish any new bonds. Given the reduction in the size of the Project Area and the decrease to the flow of annual tax increment revenues, the sale of bonds (with the new authority to do so) will be essential for the timely implementation of redevelopment activities. The indebtedness and bonds can be repaid from tax increment revenues or other funds available to the Agency, and will not require participation from the General Fund. The City may also provide assistance to the Agency to fund the Project Area, as it is able to.

Sources other than Tax Increment

Financial assistance from the City, state and federal government may be used by the Agency to fund redevelopment program expenses. The Agency will also actively solicit financial assistance in the form of grants and loans from the State and federal government. Some of the Agency's past redevelopment projects have been funded, in part, through funding provided by the City or grants from the State and federal government, or through other public agencies. For example, the construction of the new library has been funded from a combination of sources, including the proceeds of certificates of participation issued by the City and tax increment financing provided by the Agency. The Agency also expects that the federal government will provide the major funding for flood control improvements (specifically the construction of PL 566), with the Agency providing funds for the local match.

The City may also consider the creation of assessment and community facilities districts to fund redevelopment activities. Such districts will require voter approval from those that live within the boundaries of such districts.

The City also collects development impact fees. A portion of these fees are expected to be used to fund a part of the public improvement costs in the Project Area.

Tax Increment Revenues, Bonds, and Limitations

Table 13 provides an estimate of the tax increment revenues that could be generated through 2022-23, when the new tax increment limit is projected to be reached. The tax increment revenue projection is based on the following assumptions:

- New development activity shown on Table 14 that is assumed to occur based on Agency activities
- The Proposition 13 allowable inflationary adjustment of up to 2 percent annually.
- An additional growth factor of 1 percent per year to take into account the turnover of property in the Project Area.
- The reduction to taxable values of approximately $771 million in 2007-08 due to the deletion of territory.

Total gross tax increment is expected to decline in 2007-08 by approximately $8 million when the territory proposed for deletion is removed from the Project Area. These funds will be returned to the taxing entities. Table 15 shows the benefit to the taxing entities from the deletion of territory, both in 2007-08 and also through 2022-23.

Total gross tax increment shown on Table 13 is estimated at $456.7 million. Deductions have been made from this amount in order to determine the remaining amount that is available to repay Project Area obligations and provide funding for new projects. The following have been included as offsets to tax increment revenues.

Property tax administration fees, which are retained by the County, have been deducted from Table 13. The full amount of the housing set-aside has been deducted. Finally, mandatory AB 1290 tax sharing payments have been deducted, as described below.

Pursuant to 1994 legislation, AB 1290, the Agency is required to make payments to the affected taxing entities from the Project Area based on a prior amendment to the Redevelopment Plan. AB 1290 tax sharing payments are based upon growth above levels in 1999-2000 (referred to as the AB 1290 AV Base Year). The AB 1290 AV Adjusted Base Year will also need to be reduced in 2007-08 by approximately $189 million to reflect the deletion of territory.

AB 1290 pass through payments are based on the following tiers:

1. Payments to the affected taxing entities in an amount equal to 25 percent of the gross tax increment attributable to increases above the AB 1290 AV Base Year. The tax sharing payment is calculated after the amount required to be deposited in the Low and Moderate Income Housing Fund has been deducted. The net tax sharing payment is therefore equal to 20 percent.
2. In addition to the amounts paid pursuant to item (1) above and after deducting the amount allocated to the Low and Moderate Income Housing Fund, an amount equal to 21 percent of the portion of tax increments received by the Agency, which shall be calculated by applying the tax rate against the amount of assessed value by which the current year assessed value exceeds a second adjusted base year assessed value. The second adjusted base year assessed value is the assessed value of the Project Area in 2009-10.
3. In addition to the amounts paid pursuant to items (1 and 2) above and after deducting the amount allocated to the Low and Moderate Income Housing Fund, an amount equal to 14 percent of the portion of tax increments received by the Agency, which shall be calculated by applying the tax rate against the amount of assessed value by which the current year assessed value exceeds a third adjusted base year assessed value. The third adjusted base year assessed value is the assessed value of the Project Area in 2029-30. The Agency estimates that this tier of payments will not be triggered before the Agency reaches the new tax increment limit.

After reductions for the above, net discretionary tax increment is estimated at $287.5 million.

The new tax increment limit has been calculated on Table 16. The starting point for this calculation is the total cost for the Agency's programs from Table 12 of $229 million. To this amount, the Agency has added an escalator to costs of 3 percent per year. The cash flow analysis shown in the appendix of this Preliminary Report shows how these numbers were derived. The Agency has also added the cost for interest on bonds and administrative costs. The total of these items, when rounded, equals $580 million, which is the new tax increment limitation included in the Amended Redevelopment Plan. The bond limit has been estimated at $150 million.

Table13
Morgan Hill Redevelopment Agency
Ojo de Agua Project Area

PROJECTION OF INCREMENTAL TAX REVENUE

(000's Omitted)

Fiscal Year			Real (1) Property	New (2) Development	Total Real Property	Other (3) Property	Total Value	Value Over Base Of 130,715	Total Tax (4) Increment	Property Tax (5) Admin Fees	Housing Set-Aside	Mandatory AB 1290 Payment	Net Discretionary Tax Increment Revenue
2005	-	2006	2,191,199	N/A	2,191,199	200,704	2,391,903	2,261,188	23,758	319	4,752	2,361	16,327
2006	-	2007	2,256,935	0	2,256,935	206,725	2,463,660	2,332,945	24,510	329	4,902	2,511	16,768
2007	-	2008	1,648,378	8,935	1,657,313	95,251	1,752,564	1,621,849	17,110	229	3,422	1,424	12,035
2008	-	2009	1,707,032	23,632	1,730,664	98,109	1,828,772	1,698,057	17,908	240	3,582	1,583	12,504
2009	-	2010	1,782,584	66,178	1,848,762	101,052	1,949,813	1,819,098	19,173	257	3,835	1,835	13,247
2010	-	2011	1,904,224	52,293	1,956,518	104,083	2,060,601	1,929,886	20,331	273	4,066	2,226	13,767
2011	-	2012	2,015,213	68,000	2,083,213	107,206	2,190,419	2,059,704	21,688	291	4,338	2,684	14,375
2012	-	2013	2,145,709	70,040	2,215,749	110,422	2,326,171	2,195,456	23,106	310	4,621	3,164	15,011
2013	-	2014	2,282,221	72,141	2,354,362	113,735	2,468,097	2,337,382	24,589	330	4,918	3,665	15,676
2014	-	2015	2,424,993	74,305	2,499,298	117,147	2,616,444	2,485,729	26,138	351	5,228	4,189	16,372
2015	-	2016	2,574,277	48,929	2,623,206	120,661	2,743,867	2,613,152	27,470	368	5,494	4,638	16,969
2016	-	2017	2,701,902	51,857	2,753,759	124,281	2,878,040	2,747,324	28,872	387	5,774	5,112	17,599
2017	-	2018	2,836,371	63,079	2,899,450	128,009	3,027,460	2,896,744	30,434	408	6,087	5,640	18,299
2018	-	2019	2,986,434	68,172	3,054,606	131,850	3,186,455	3,055,740	32,094	430	6,419	6,201	19,044
2019	-	2020	3,146,244	4,892	3,151,136	135,805	3,286,941	3,156,226	33,146	445	6,629	6,556	19,517
2020	-	2021	3,245,670	0	3,245,670	139,879	3,385,549	3,254,834	34,179	458	6,836	6,904	19,980
2021	-	2022	3,343,040	0	3,343,040	144,076	3,487,116	3,356,401	35,242	473	7,048	7,263	20,458
2022	-	2023	3,443,331	0	3,443,331	148,398	3,591,729	3,461,014	16,924	262	3,460	3,624	9,578
Cumulative Total									**456,674**	**6,160**	**91,410**	**71,579**	**287,526**

(1) Prior Year Real Property increased by 3 percent per year.

(2) See Table 14, Schedule of New Development.

(3) Includes the value of secured and unsecured personal property, and state-assessed railroad and non-unitary property.

(4) Based on the application of Project Area tax rates to incremental taxable value. Also inlcudes unitary revenues based on allocation for 2004-05.

(5) Amount shown reflects estimated property tax administrative fees charged by County at 1.3%.

Table 14
Morgan Hill Redevelopment Agency
Ojo de Agua Project Area

NEW DEVELOPMENT ACTIVITY

Development	Estimated Value (1)	Estimated Timing (1)
TBI Office Development: This 73,000 square foot office development is proposed to be built along Cochrane Road.	$11 million	Projected to add value to the 2007-08 and 2008-09 tax roll.
Downtown Mixed Use: This project is intended to include 10,000 square feet of retail and seven condominium units.	$6 million	Value is expected to be added to the 2007-08 and 2008-09 tax rolls
Infill Development: A total of 234,000 square feet of additional commercial development is projected to occur in the Project Area. An additional 400 housing units are also projected to occur.	$335 million	New construction projected to add value through 2020
Morgan Hill Business Park: Additional development in the business park could include another 750,000 square feet of space.	$75 million	May occur between 2010 and 2020
Redevelopment Sites: A number of sites in the downtown and along Monterey Avenue could be redeveloped in the future. A total of 200 housing units and 250,000 square feet of commercial development has been assumed.	$118 million	New value projected to be added between 2010 and 2020

(1) The value and timing shown are estimates only and will likely vary.

Table 15
Morgan Hill Redevelopment Agency
Ojo de Agua Project Area
Impact on Taxing Entities- Deletion Area (1)
(000's Omitted)

Taxing Entity	Post-ERAF (2) Percentage Share	First Year Amount	Total Through 2022-23	(3) NPV
Santa Clara County	14.19%	1,140	22,978	14,378
County Library	2.64%	212	4,272	2,673
City of Morgan Hill	10.75%	864	17,407	10,892
Morgan Hill Unified	44.57%	3,580	72,163	45,154
Gavilan Comm College	5.67%	455	9,173	5,740
County Office of Education	3.42%	274	5,530	3,460
Santa Clara Valley Water Dist E-1	0.33%	27	541	338
Santa Clara Valley Water District- South	1.29%	104	2,094	1,310
Santa Clara Valley Water District - General	0.18%	14	285	179
Bay Area Air Quality Management Dist	0.19%	15	306	191
Loma Prieta Res Cons	0.04%	3	65	40
SCVWD Zone W-3	1.01%	81	1,643	1,028
SCVWD St Water	0.50%	40	808	506
ERAF	15.22%	1,223	24,646	15,422
TOTAL	**100.00%**	**8,033**	**161,911**	**101,312**

(1) Impact of deleting territory. Shows the estimated amount of tax increment to be returned to the taxing entities.
(2) Based on Post-ERAF shares.
(3) NPV calculated at 5% discount rate.

Table 16
Morgan Hill Redevelopment Agency
Ojo de Agua Project Area

TAX INCREMENT AND BOND LIMITS
(000's Omitted)

Total Project Costs (1)	$229,000
Escalation of Costs (2)	66,533
Interest on Bonds (3)	44,000
Administrative Costs	46,000
Plus Tax Increment Received through 2004-05 (4)	194,913
Total	580,446
Tax Increment Limit - Rounded	**580,000**
Bond Limit - Rounded	**150,000**

(1) Combined total of costs shown on Table 12.
(2) Costs escalated at 3 percent per year, as shown on cash flow table contained in appendix.
(3) Estimate is based on total of $92 million in bonds. Bonds assumed to be paid off early, per cash flow table in appendix.
(4) Amount received by Agency, less Statutory Payments and admin fees that are not subject to the tax increment limit pursuant to the amendment.

8.3 PROPOSED FINANCING METHOD AND ECONOMIC FEASIBILITY

The proposed method of financing redevelopment and the economic feasibility of the Project Area have been summarized on Table 17. A complete cash flow has also been provided in Appendix B.

Table 16 compares the future projected tax increment revenues of the Project Area, plus other resources, to the existing obligations and program expenditures. Existing obligations include:

- AB 1290 Mandatory Tax Sharing Payments; and
- Administrative costs for the Project Area

The feasibility analysis also includes all of the expenditures needed to implement the Economic Revitalization Program and the Public Improvements Program and the Housing Program. The cost for these programs are based on the amounts shown on Table 12, adjusted by a 3 percent per year factor for inflation.

It should be noted that the analysis shown on Table 16 and Appendix B is based on one set of assumptions for continued implementation of redevelopment. It should not be considered the only means to continue to finance redevelopment of the Project Area. The analysis does indicate that the Project Area will continue to be financially feasible given the set of assumptions that underlie the projections and the proposed amendments to the financial and time limits. The primary assumptions in this regard are that:

1. The tax increment and bond limits will be increased as proposed
2. The costs for redevelopment activities are as projected
3. New development activity will occur in the Project Area as the Agency continues to remove impediments to development.

It is assumed in the analysis that the Agency will address and mitigate remaining blighting conditions discussed in previous parts of this Report throughout the duration of the redevelopment program. It is assumed that the Agency's efforts through the Economic Revitalization Program will serve as a catalyst for the generation of revenue necessary for the continued implementation of the redevelopment program. As the remaining deteriorated, aged and obsolete structures and other blighted properties are recycled or rehabilitated as a result of Agency activities, the annual flow of tax increment revenue will grow.

One of the key assumptions that underlay the cash flow analysis presented in Appendix B is that the Agency will issue tax allocation bonds in the future. The deletion of territory from the Project Area will reduce the annual flow of tax increment by over $8 million per year. In order to continue to implement redevelopment activities in a timely manner, it is assumed that the Agency will sell tax allocation bonds. This will allow the Agency to generate a large amount of capital to fund projects. Bond issues totaling over $95 million are assumed to be issued in the future.

Table 17 shows that projected tax increment revenues and other resources will exceed expenditures. When the Agency reaches the new tax increment limit, it is estimated that the Agency would have a cash balance of $10.9 million. This balance is the Project Area's hedge against higher than expected costs or revenues that fall short of projections. Given this, the Project Area will continue to be economically feasible.

Table 17
Morgan Hill Redevelopment Agency
Ojo de Agua Project Area

FINANCIAL FEASIBLITY ANALYSIS
(000's Omitted)

Resources	
Beginning Balance	$8,492
Tax Increment Revenues	454,468
Bond Proceeds	90,220
Investment Earnings	6,820
Total Resources	$560,000
Expenditures	
Mandatory AB 1290 Tax Sharing	72,405
Bond Debt Service (2)	81,111
Early Bond Pay Off (3)	55,000
Economic Revitalization	81,317
Public Improvements & Facilities	122,806
Housing Progams	91,410
Administrative Expenses	45,027
Total Expenditures	$549,076
Ending Balance	**$10,925**

(1) Tax increment less property tax admin fees.
(2) Includes principal, interest, and issuance costs.
(3) Bonds assumed to be paid off sooner than the actual maturity schedule for bonds.

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APPENDIX A

List of Preparers

ERNEST GLOVER

President, GRC Redevelopment Consultants

As President of GRC Redevelopment Consultants, Inc. since 1993, Mr. Glover has managed over 150 Redevelopment Plans and land use programs. He provided the economic, demographic and fiscal information for this report.

PAUL SCHOWALTER

Principal, GRC Redevelopment Consultants

Mr. Schowalter acted as Project Manager for this proposed Project. Duties for this Project include field observations and document preparation. Since joining GRC Redevelopment Consultants in 1989, he has completed over 100 Redevelopment Plans and amendments.

DON FRASER

President, Fraser & Associates

Mr. Fraser prepared the financial analysis that is included in the Report. Fraser & Associates specializes in financial analysis for redevelopment agencies, and has worked on various financings throughout California for the past 14 years. Mr. Fraser has assisted in the amendment or adoption of over 30 redevelopment plans.

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APPENDIX B

Cash Flow Analysis

Appendix B
Morgan Hill Redevelopment Agency
Ojo de Agua Project Area

CASH FLOW ANALYSIS

(000's Omitted)

	2005-2006-	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	2014-2015
Resources										
Beginning Balance	$8,492	$2,290	$323	$70,622	$54,470	$24,418	$3,076	$2,451	$24,372	$16,190
Adjusted Tax Increment Revenues		24,181	16,881	17,668	18,916	20,059	21,397	22,796	24,259	25,788
Bond Proceeds	0	0	64,810	0	0	0	0	25,410	0	0
Investment Earnings	300	69	10	2,119	1,634	733	92	74	731	486
Other Revenue Sources	0	0	0	0	0	0	0	0	0	0
Total Resources	$32,232	$26,540	$82,023	$90,409	$75,020	$45,209	$24,565	$50,731	$49,362	$42,463
Expenditures										
Mandatory AB 1290 Tax Sharing	2,361	2,511	1,424	1,583	1,835	2,226	2,684	3,164	3,665	4,189
Bond Debt Service	0	0	0	5,126	5,126	5,126	5,126	5,126	7,438	7,438
Early Bond Pay Off	0	0	0	0	0	0	0	0	0	0
Economic Revitalization	2,130	3,032	3,752	6,687	13,444	11,876	3,916	8,861	9,150	8,225
Public Improvements & Facilities	19,036	13,412	371	16,456	23,783	16,182	3,313	1,768	5,099	9,003
Housing Programs	4,752	4,902	3,422	3,582	3,835	4,066	4,338	4,621	4,918	5,228
Administrative Expenses	1,663	2,361	2,431	2,504	2,579	2,657	2,737	2,819	2,903	2,990
Total Expenditures	$29,942	$26,217	$11,401	$35,939	$50,602	$42,134	$22,114	$26,358	$33,173	$37,073
Ending Balance	**$2,290**	**$323**	**$70,622**	**$54,470**	**$24,418**	**$3,076**	**$2,451**	**$24,372**	**$16,190**	**$5,391**

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